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Connecticut Bar Association Committee on Professional Ethics
Advance Of Funds To Client By Third Party

TEXT: The requester has asked for the opinion of this committee concerning whether it would be unethical for his office to participate in or to encourage his clients to participate in a program in which a Florida corporation has offered to advance money to personal injury claimants secured by the claimant's potential recovery in the personal injury claim. The committee has reviewed information received from both the requester and from the Florida corporation, which we shall call, for purposes of this Opinion, "XYZ, Inc."

The requester received an unsolicited mailing from XYZ, Inc. The mailing included an introductory letter which read, in toto, as follows:

> SUBJECT: HOW TO EARN HIGHER FEES via HIGHER SETTLEMENTS
>
> As Executive Vice President and Counsel for [XYZ, Inc.], I have the opportunity of speaking with Personal Injury Attorneys around the country. The one significant fact that seems to stand out is the frequency in which their clients badger them to accept a "quickie" settlement instead of allowing sufficient time for proper negotiations. The main reason for this being that, unable to work due to accident or personal injury, they are getting further into debt and finding it harder to meet day-to-day living expenses.
>
> THIS IS WHERE [XYZ, Inc.] CAN BE OF SUBSTANTIAL BENEFIT TO BOTH YOU AND YOUR CLIENT. [XYZ, Inc.] IS IN BUSINESS TO ADVANCE FUNDS AGAINST A PORTION OF THE CLIENT'S FUTURE SETTLEMENT.
>
> With the wolf removed from their door, the client is more willing and able to allow you to try the case as you see best.
>
> No credit checks are required, our service is fast and confidential. Since this is not a loan, in the event there is no settlement, or insufficient settlement, the client owes us nothing. To receive a copy of the application for your client, please complete the following and fax it to me at (000-000-0000.) Please tell your secretary you are expecting this material. (bold print in original)

Underneath the body of this letter is a tear-off application form requesting the name, address, phone number and fax number of the person to whom client application forms should be sent.

As part of the application process, the client is required to fill out and/or execute two forms. The first of these is called a "CLIENT'S AUTHORIZATION FOR RELEASE OF INFORMATION TO (XYZ, Inc.)." This document is a client authorization which directs the attorney (1) to release to XYZ, Inc. all relevant information including medical records, demands, offers, counter-offers, medical bills, liens and letters of protection in the attorney's file related to the client's claim and (2) to cooperate with XYZ, Inc. to determine

if the client might qualify for "interim advance financial assistance against any future settlement" the client may receive.

The second of these forms is the application itself, which is entitled, "REQUEST FOR INFORMATION." In this document, the claimant is asked to provide background information concerning the bodily injury involved, the treating physicians, collateral source payments, present compensation being received, the date and a description of the accident or injury, the amount of funds being requested, an estimate of the value of the claim and the name, address, telephone number and fax number of the claimant's attorney.

The cover letter forwarded with the application explains that, "should there be no settlement, or insufficient settlement, the client applicant will owe us nothing. XYZ, Inc. assumes 100 percent of the risk in advancing such funds, however, no funds can be advanced in which an offer of settlement has already been made."

The cover letter also alludes to XYZ, Inc.'s fees, which are based upon the amount of capital advanced, the type and severity of injury involved, and the length of time to trial and/or settlement. These fees, also called a "service charge", typically run from 8 to 10 percent a month. Parenthetically, XYZ, Inc. explains that its "service charge" is not usurious because the advance is not, strictly speaking, a loan in that there is no obligation to repay the advance if the net from the settlement or judgment is insufficient or nonexistent.

XYZ, Inc. reviews the client's application upon receipt. If the application is accepted, XYZ, Inc. proffers an agreement to the client to advance a small portion of the claim's estimated value, usually in the range of 10 percent.

The terms of the written agreement require the client to agree to repay the principal balance of the advance and the monthly service charge to XYZ, Inc. from the proceeds of any settlement or judgment after first deducting the attorney's fees and the "outstanding medical expenses." The client's obligation to repay XYZ, Inc. is expressly limited to the net of the claim after "first paying any and all expenses connected therewith." The client also agrees to pay XYZ, Inc. without "demand" any reasonable attorney's fees and all costs and other expenses incurred in collecting or compromising any indebtedness arising out of the agreement. The agreement further states that it is governed by and construed under Florida law that XYZ, Inc. shall have a general lien against any settlement proceeds recovered against the alleged tortfeasor and that the client, pursuant to the agreement, authorizes and directs his attorney to make any payments due under the contract to XYZ, Inc. The agreement concludes by assigning to XYZ, Inc. the client's rights against the purported tortfeasor in the event that the client abandons the claim.

The client is also required to sign a letter of protection which authorizes and directs his or her attorney to withhold an appropriate sum from the net of the settlement or judgment and to forward payment from that amount to XYZ, Inc. Moreover, the letter of protection grants XYZ, Inc. a lien against "any and all proceeds of any settlement, judgment or verdict" which may be paid to the client or to his or her attorney to the extent "of the amounts due or owing to (XYZ, Inc.) pursuant to my agreement with them."

The attorney is asked to perform the following functions in regard to the transaction described above (hereinafter the "XYZ, Inc. Transaction"). After introducing the client to XYZ, Inc., and after the client has authorized him or her to do so, the attorney forwards materials related to the client's claim to XYZ, Inc. The committee infers that the attorney provides the monetary estimate of the client's claim as requested in the application. Thereafter, there may be further discussions between the attorney and XYZ, Inc. as a result of the client's written direction to the attorney to cooperate "to enable (XYZ, Inc.) to determine if I might qualify for interim advance financial assistance against any future settlement I might receive." After the application has been accepted, the attorney subscribes to the client's signature on a letter of protection running in favor of XYZ, Inc. In this letter of protection, the attorney agrees to "observe all terms of the above, and agrees to withhold sufficient sums from any settlement, judgment or verdict to pay XYZ, Inc. in accordance with (client's) agreement with them." Finally, after settlement or judgment has been received and netted out, the attorney is asked to withhold the amount owed to XYZ, Inc. and forward this amount to XYZ, Inc.

[illegible] This rule states that, "A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation." As the Scope of the Rules reflects, the use of the word "shall" in Rule 1.4(b) indicates that this rule imposes an imperative, affirmative obligation concerning communication. Rules which use the word [illegible]

As mentioned above, the requester has asked if it would be "unethical" for his office "to participate in such an arrangement or to encourage our clients to do so."

[illegible]

[illegible] the attorney's fee and other expenses have been subtracted therefrom. The attorney receives no fee per se from XYZ, Inc., although the attorney's fee is protected in the XYZ, Inc. Transaction.

The XYZ, Inc. Transaction described above creates an even greater danger of violating Rule 2.1. As [illegible]

[illegible] the case his or her way, this portion of Rule 2.1 would be violated. As Hazard and Hodes points out, "The first sentence of Rule 2.1 is a mandatory rule of conduct. The language 'shall exercise independent professional judgment' is taken from Canon 5 of the Code of Professional Responsibility and also evokes the duty to avoid improper influence by others (Rule 1.7), whether those 'others' are third parties, or the lawyer himself." Hazard and Hodes, at 500. [illegible]

However, the committee believes that before considering entering into the XYZ, Inc. Transaction, the lawyer should seriously consider the implications of the following Rules of Professional Conduct.

[illegible]

[illegible] in (the attorney's) file relating to (the attorney's) representation for recovery of damages," that document, in and of itself, does not satisfy the requirements of Rule 1.6(a). As stated above, Rule 1.6(a) prohibits the attorney from disclosing information relating to the representation unless the client consents after "consultation." The Terminology section of the Rules of Professional Conduct defines "consultation" as "communication of information reasonably sufficient to permit the client to appreciate the significance of the matter in question." Although the committee does not opine on questions of law, it would seem that the kind of "consultation" necessary to permit the client to appreciate the significance of the matter in question should include a discussion of, among other things, whether the disclosure by the attorney to XYZ, Inc. of the information requested might constitute a waiver of the attorney-client privilege, or render discoverable otherwise undiscoverable information. Therefore, to avoid violating Rule 1.6(a) under these circumstances, an attorney would [illegible] "Loyalty is an essential element to the lawyer's relationship to a client."

Another rule which should be considered by any lawyer considering participating in or encouraging his or her client to participate in the XYZ, Inc. Transaction is Rule 1.7(b). This rule states, in pertinent part, that:

> A lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to . . . a third person, or by the lawyer's own interests, unless:
>
> (1) [illegible]
>
> (2) the client consents after consultation.

[illegible]

[illegible] need to be a mathematician to realize that, in a relatively short period of time, the client owes to XYZ, Inc. an amount equal to or greater than the principal

initially advanced. The sales pitch found in this solicitation letter is that the advance made by XYZ, Inc. to the client removes financial pressure from the client, and therefore allows the attorney the freedom to try the case as the attorney desires. Reviewed in this fashion, the transaction proposed may result in a violation of Rule 1.7(b), which is excerpted above.

A lawyer who participates in the XYZ, Inc. Transaction in the manner described above, may help to create a situation in which the lawyer's own interest in collecting a larger contingent fee materially erodes the undivided loyalty which the lawyer owes to his or her client. Although the XYZ, Inc. advance may satisfy the client's pressing need for cash, the 8 to 10 percent monthly service charge soon becomes a millstone around the client's neck. If a Connecticut lawyer were to encourage his or her client to enter into an XYZ, Inc. Transaction or, simply present the XYZ, Inc. materials to his or her client for the purpose of allowing the attorney the opportunity to control the decision-making process, the lawyer's representation of his or her client would be materially limited by the lawyer's own interest. The exceptions found in subsection (1) and (2) of Rule 1.7(b) would not rescue the attorney from a Rule 1.7(b) violation unless (1) the attorney "reasonably believes" that the representation will not be adversely affected and (2) the client were to consent after consultation. In the Terminology section of the Rules of Professional Conduct, the phrase "reasonably believes" is defined to mean that the lawyer actually believes the matter in question and that the circumstances are such that the belief would be reasonable in the eyes of a prudent and competent attorney. If the attorney can vault that hurdle, the attorney must secure the client's consent after consultation. As mentioned above, the Terminology section defines "consultation" to denote communication of information reasonably sufficient to permit the client to appreciate the significance of the matter in question."

Further, though the committee does not issue legal opinions, it notes that any attorney who considers participating in or encouraging his or her client to participate in an XYZ, Inc. Transaction should review all potentially applicable rules, statutes and cases to determine whether the transaction is illegal or violative of public policy. For example, in light of the XYZ, Inc. Transaction's requirement that the claimant must assign his or her rights to XYZ, Inc. if the claimant chooses not to pursue the alleged tortfeasor, a practitioner should review *Dodd v. Middlesex Assurance Company, 242 Conn. 375, 382 (1997).* This case describes in detail Connecticut's proscription against the assignment of personal injury actions. By way of illustration, but not of limitation, the committee directs any practitioner considering participation in an XYZ, Inc. Transaction to the case of *Rice v. Farrell, 129 Conn. 362; 28 A.2d 7 (1942).* This case holds that, "the common law doctrines of champerty and maintenance as applied to civil actions have never been adopted in the state," but that the touchstone used in evaluating a similar transaction is whether it is "against public policy." In Rice, a third party offered to finance a lawsuit to be instituted by a plaintiff to recover certain real property, with the following understanding: If the suit were unsuccessful, the plaintiff would not need to reimburse the third party; but if the suit were successful, the third party would be able to buy the property from the plaintiff for fair market value minus the expenses of the litigation. In this case, the Supreme Court stated that, "while a stranger to litigation may properly assist a poor person to assert his rights, such assistance is not permissible when the stranger is to share in the proceeds of the action . . . the agreement before us is against public policy and therefore, as between the parties to it, unenforceable." See also *Robertson v. Town of Stonington, 1999 WL 99214* (Conn. Super February 17, 1999.)

Similarly, before a practitioner recommends that his or her client enter into the XYZ, Inc. Transaction, the practitioner should conduct his or her own analysis of, among other issues, (1) whether the XYZ, Inc. Transaction complies with state and federal laws relating to truth-in-lending, (2) whether the XYZ, Inc. Transaction complies with state and federal laws relating to usury, (3) which choice of law rules would apply to the XYZ, Inc. Transaction, and (4) all aspects of the XYZ, Inc. Transaction under applicable contract law. Before an attorney advises a client whether or not to participate in a program such as the one proposed by XYZ, Inc., very careful consideration should be given to the problems discussed above.

In considering whether to participate and/or encourage his or her client to participate in the XYZ, Inc. Transaction, an attorney should also bear in mind that an attorney-client relationship gives rise to a fiduciary relationship. A fiduciary relationship is characterized by a unique degree of trust and confidence between the parties, one of whom has superior knowledge, skill or expertise and is under a duty to represent the interests of the other. *Dunham v. Dunham, 204 Conn. 303, 319-322 (1987).*